

Foreign Acquisition Playbook

By Will Chuchawat

In the past few years, an increasingly large number of Chinese companies have attempted to expand into foreign markets. But such expansion is easier said than done: in the past, Chinese companies have been better passive investors than acquirers. This article offers tips on identifying acquisition targets, making acquisitions happen, and making them succeed. It shows ways to maximize the odds that a deal will not be blocked and that it will create value.

1. Identifying targets

There are two basic approaches to entering a foreign market. The first is to enter the foreign market with low prices and slowly build up brand-name recognition and customer loyalty. This is what Japanese and Korean automakers did successfully in the 1980's. The second is to buy an established foreign company. Most Chinese companies lack brand-name recognition and international distribution channels. With rapid internationalization, Chinese companies do not have the luxury of spending a decade developing their brands as the Japanese did. Thus, acquiring a foreign company is nowadays generally preferable.

Acquirers generally look for companies that complement existing busi-

nesses. For Chinese companies, attractive foreign enterprises are those with well-known brands and international distribution channels. Some companies can also benefit from strong research and development capabilities.

In the automotive sector, acquisition opportunities are available because slumping American automakers have been divesting non-core assets in the face of rising fuel costs. Although Chinese companies have long enjoyed inexpensive labor, domestic opportunities have decreased due to increasing joint venture investments by foreign



automakers, and increasing foreign competition as a result of decreasing import tariffs on cars (now at 25%) and auto parts (10%). News broke out on 26 June 2008 that Shanghai Automotive Industry Corporation ("SAIC") was in negotiations over a possible purchase of Volvo cars in Sweden. Volvo is the

epitome of the safe and dependable car. An acquisition of Volvo would improve the global image of SAIC, and give it a global distribution network, advanced technology, and strong research and development capabilities that can benefit the entire company. Some manufacturing can be moved to China to take advantage of lower manufacturing costs and economies of scale, as was done after Nanjing Automotive Group's (later acquired by SAIC) takeover of Britain's then-defunct MG Rover in 2006.

2. Completing a Deal

Once a target has been identified, companies should consult with the right professionals. When you are an acquirer looking to deal with Western companies, it makes all the difference to have a professional who is experienced in dealing for and against Western companies. Those types of professionals will be able to anticipate what a Western party is thinking, how they will react, and what your approach should be.

In a cross-border deal, you will also have to consider that opposition to the deal can stem from both within and outside the company being acquired. Such opposition usually only arises in the largest size deals or in sensitive

industries. Most transactions will not cause the same type of uproar as you may have read about in the press. Of course, if there is government opposition, then that will usually be the end of that deal. In the past, unprepared Chinese companies have been caught red-faced when deals elicited popular contempt in foreign countries or were blocked for non-business reasons. Professional advice becomes especially crucial when an acquisition target is profitable or owns venerable brands: deals in these situations tend to attract scrutiny. In unfavorable situations, experienced professionals can navigate through unwanted attention and structure the deal to assuage concerns.

3. Making a Deal Succeed

After the deal is complete, acquirers face the challenge of integrating two companies from different countries. Although this is never easy, there are two ways to alleviate integration difficulties.

The first is to recognize and bridge cultural differences. When foreign businesspeople come to China, they adopt local customs to demonstrate their respect and perceptiveness. Indeed, foreign buyers and renters of real property in China often consult fengshui masters, just as the Chinese tend to do. Conversely, managers of Chinese companies expanding abroad should be aware of cultural differences, and pay respect to both cultures. For example, the founders of many Chinese companies tend to be highly entrepreneurial and make most decisions in their companies. Managers of these companies that are investing in America should understand that Americans value analyses and processes. Managers of those investing in Japan should understand that Japanese businesspeople value consensus.

The second is to partner with a for-

ign company already operating in the country of the acquired company. In particular, if the acquired company was sold by a parent company, then the deal can be structured to force the seller to retain a minority stake for a number of years. This gives the seller an incentive to ensure a smooth transition, and the acquirer a mentor in an unfamiliar market. The best known example can be found in the IBM-Lenovo deal. When IBM sold Lenovo its personal computing business, it retained an 18.9% equity stake for five years. This likely helped Lenovo's growth on the world stage.

Every deal is different, and no one formula will work the same way. The first step is to understand why you are

looking to go abroad. Although business executives are the best at producing the vision for expansion, a good professional can help you plan at this stage to make sure that the vision is practical and can be achieved. Once the plan is in place, professionals will carry the load to get the deal done, to make sure you have protection in case the deal goes wrong in the future, and to make sure that you considered all of the risks beforehand. Finally, it will be up to the business people to have an integration plan in place before the deal is done, and to make sure that transition is smooth and successful. It all starts with consulting with the right professionals early on. **CBF**

(The author of this article is a senior attorney of Sheppard Mullin Richter & Hampton LLP)

